Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, DC 20554

In the Matter of	)	
	)	WC Docket No. 02-313
2002 Biennial Regulatory Review	)	

REPLY COMMENTS OF AT&T CORP.

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Pursuant to the Commission's Public Notice,[1] AT&T Corp. ("AT&T") submits these reply comments in opposition to the anticompetitive regulation repeals and modifications sought by various incumbent local exchange carriers ("ILECs") and other commenters.

INTRODUCTION AND SUMMARY

The incumbent local exchange carriers seek to turn the biennial regulatory review process into a free-for-all, in which they roll out lengthy wish lists of regulatory reforms, seeking to remove the remaining safeguards against their exercise of market power. Many of these issues are already pending in other dockets (and, indeed, some have not even been briefed yet in those proceedings), and thus are inappropriate for consideration here. The incumbents' frivolous attempts to bootstrap this biennial review proceeding into almost full deregulation of their monopoly services has no basis in law or policy and is a clear abuse of the Commission's processes.

The biennial review mandate of the 1996 Act requires the Commission to assess whether any of its existing regulations are "no longer necessary in the public interest as the result of

[1] Public Notice, *The Commission Seeks Comments In 2002 Biennial Review Of Telecommunications Regulations Within The Purview Of The Wireline Competition Bureau*, FCC 02-267, WC Docket No. 02-313 (released September 26, 2002).

meaningful economic competition."[2] To the extent that the Commission determines that meaningful competition has rendered particular regulations no longer "necessary in the public interest," the Commission may "repeal or modify" those regulations.[3] The incumbent LECs' requests for deregulation do not even attempt to satisfy the statutory standard. In fact, the incumbents make no attempt whatsoever to demonstrate that new "meaningful economic competition" has deprived them of the market power – and the incentives and ability to abuse that market power at the expense of consumers and competition – that the regulations the incumbents seek to evade were designed to detect and prevent.

Verizon goes even further, and proposes a bizarre interpretation of Section 11 under which the Commission must accede to every demand on its wish list by December 31 of this year (including resolution of the Triennial UNE Review and the broadband regulation proceedings) or face certain reversal. According to Verizon, the biennial review process *requires* the Commission to conduct the equivalent of a new rulemaking proceeding and develop clear and substantial evidence of the indispensability of any – and every – rule that the Commission wants to retain. As demonstrated in Part I of these comments, however, Verizon's attempt to rewrite the statute is entirely baseless. Congress and the courts have long understood the phrase "necessary in the public interest" in the context of general rulemaking provisions like Section 11 to confer broad authority to adopt (or retain) rules that are useful or appropriate in the public interest.

The remaining sections of these comments address several of the specific groups of regulations that the incumbent LECs seek to modify or repeal. Part II addresses USTA's

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[2] 47 U.S.C. § 161(a)(2).

proposal to essentially abolish the Commission's accounting and record keeping rules. USTA does not offer any evidence that meaningful economic competition has developed that would remove their usefulness. The Commission already has begun the process of carefully reviewing its existing accounting rules by establishing a Federal-State Joint Conference Board to review the Commission's existing accounting safeguards rules in order to "help restore public confidence in the telecommunications industry by improving regulatory reporting requirements."[4] The Commission should continue that process by retaining – and strengthening – its accounting rules, not by repealing them. In all events, now clearly is not the time to release the incumbent LECs, which still maintain overwhelming market power, from the accounting requirements designed to detect and thwart their ability to wield that market power to the detriment of consumers and competition. Accordingly, the Commission's current accounting safeguards – which deter incumbent LECs from acting on their strong anticompetitive incentives by prohibiting such conduct, and by requiring LECs to provide information that allows the Commission and other entities to detect such behavior – are no less (and, indeed, more) vital today as they were when initially adopted by the Commission.

Part III addresses proposals to modify certain universal service rules – in particular, proposals to add equal access to the definition of universal service and to modify the Rural Health Care Support Mechanism in ways that would increase the size of the universal service fund. Both of these proposals should be rejected.

Part IV addresses various proposals concerning access charges. First, the Commission should enforce, not repeal, the "all-or-nothing" rule, which requires LECs to convert to price

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[3] *See id.* § 161(b)

caps whenever it acquires an exchange governed by price caps. The Commission should not permit all LECs to file contract-based tariffs, nor should it adopt any of the other one-sentence requests for access-related reforms advocated by USTA. The Commission should also reject NECA's requests for modification of the rules relating to Subscriber Line Charges for high capacity lines and cash working capital allowances.

Finally, Part V addresses a number of additional regulations that the incumbent LECs urge the Commission to repeal, but that remain critical to protecting consumers and competition, including undbundling requirements, pole attachment rules, local number portability rules, and the section 214 exemption rules for international carriers. As demonstrated below, all of these proposals should be rejected, because they are not appropriately addressed in this proceeding, and lack merit.[5]

I. SECTION 11 REQUIRES ONLY THAT THE COMMISSION REVIEW ITS REGULATIONS AND NOT THAT THE COMMISSION REPEAL ALL REGULATIONS THAT IT DOES NOT SPECIFICALLY FIND ARE REQUIRED.

Verizon advocates a construction of Section 11 of the 1996 Act that would effect a sea change in administrative law and do unprecedented harm to the public interest. According to Verizon (at 7), the Commission must, in each even-numbered year, repeal all regulations that it does not specifically find to be "required." Furthermore, Verizon contends, no such finding is possible with respect to any regulation unless the Commission marshals substantial record evidence of absolute necessity that is specific to that regulation.

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[4] *See* Order, *Federal-State Joint Conference On Accounting Issues*, FCC 02-240, WC Docket No. 02-269 (released September 5, 2002) ("Joint Board Accounting Order").

[5] These comments to do not (and need not) address every meritless proposal to eliminate rules offered by the LECs. Rather these comments focus on the proposals that would be most detrimental to consumers and competition.

Verizon's claim is made of whole cloth. Section 11 simply directs the Commission to evaluate whether existing regulations that the Commission promulgated to protect the public and has already supported with substantial evidence (generally evidence that the regulation would aid in discouraging market power abuses by Verizon and other local monopolists) remain "necessary in the public interest." Verizon excises the words "in the public interest," and then asserts that the sole remaining word "necessary" *must* be interpreted as "required." Not content to stop there, Verizon asserts (at 6-9) that Section 11's command that the Commission undertake a review of its regulations in every even-numbered year must be read to mean that the Commission must not only initiate a separate review of each and every one of its regulations in each even-numbered year, but that, in the certain event that it is unable to *complete* its review and build a record of substantial evidence with respect to every single regulation by the end of the year in which the review is initiated, the Commission must immediately repeal *every* regulation for which review has not yet been completed. But as the Commission itself has expressly recognized, this absurd construction is inconsistent with both the statutory language and prior precedent, and is antithetical to the core public interest goals underlying the Communications Act and the 1996 Act amendments.

A. Contrary To Verizon's Assertion, A Regulation That Is Conducive Or Useful To The Public Interest Is "Necessary In The Public Interest."

Verizon's entire position is based on a statute that does not exist. Section 11[6] asks the Commission to evaluate whether its existing regulations are "necessary in the public interest." The courts have consistently interpreted this phrase broadly to mean "useful or appropriate" to

[6] 47 U.S.C. § 161.

the public interest rather than "required."[7] Congress is, of course, presumed to know how terms have been judicially interpreted.[8] Thus, when Congress drafted Section 11 to include the phrase "necessary in the public interest" – a term of art that the Supreme Court has concluded that Congress was well aware of at the time of the 1996 Act[9] – rather than use the single word "necessary" as it did elsewhere in the Act,[10] Congress clearly intended a different standard.[11] Congress thus expressly and intentionally included the broad meaning of that phrase and thereby granted to the Commission the broad discretion that the phrase "necessary in the public interest" has always conferred.

For this reason, the cases that Verizon cites (at 4 & nn. 11-13) regarding interpretation of the term "necessary" in the context of the Act's provisions regarding proprietary UNEs, collocation, and preemption simply are inapplicable.[12] The relevant statutory provisions at issue

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[7] *See, e.g.*, *National R.R. Passenger Corp.* v. *Boston & Maine Corp.*, 503 U.S. 407, 418-19 (1992) (affirming ICC interpretation of "required" to mean "useful or appropriate"; citing *M'Culloch* v. *Maryland*, 17 U.S. 316, 413 (1819) as "a choice of interpretations with some parallels to this one [which] read the word "necessary" to mean "convenient, or useful"); *Texaco, Inc.* v. *FERC*, 148 F.3d 1091, 1097 (D.C. Cir. 1998). *See also AT&T Corp.* v. *Iowa Utils. Bd*., 525 U.S. 366, 378 n.5 (reading "necessary in the public interest" as a "general grant of rulemaking authority").

[8] *See Lorillard* v. *Pons*, 434 U.S. 575, 583 (1978) ("where words are employed in a statute which had at the time a well-known meaning at common law or in the law of this country they are presumed to have been used in that sense unless the context compels to the contrary" (quotaiton omitted)).

[9] *AT&T*, 525 U.S. at 378 n.5.

[10] *See, e.g.*, 47 U.S.C. § 251(d)(2)(A), § 251(c)(6), and § 253(d).

[11] *See, e.g.*, *Texaco, Inc.* v. *FERC*, 148 F.3d 1091, 1097 (D.C. Cir. 1998) (interpreting FERC statute which permits regulation "necessary in the public interest" as "requir[ing] only that [FERC] point to a generic public interest in favor of a proposed rule"); *see also AT&T Corp.* v. *Iowa Utils. Bd.*, 525 U.S. 366, 378 n.5 (1999) (noting that 1996 Act was enacted in light of and with full knowledge of 47 U.S.C. § 201(b), which is a "general grant of rulemaking authority" permitting the Commission to "'prescribe such rules and regulations as may be necessary in the public interest.'"); *NBC* v. *FCC*, 319 U.S. 190, 219 (1943) (stating that the standard of "public interest, convenience, or necessity" from the Act "game the Commission not niggardly but expansive powers").

[12] Verizon cites but one decision that actually involved the relevant term "necessary in the public interest." *Fox Television Stations, Inc.* v. *FCC*, 280 F.3d 1027, 1050 (D.C. Cir. 2002) ("*Fox I*"), *modified in relevant part on reh'g*, 293 F.3d 537 ("*Fox II*"). And, as Verizon concedes, the court of appeals, in response to rehearing petitions from the Commission and others, *retracted* the portion of the decision upon which Verizon relies. *Fox II*, 293 F.3d at 541. The court concluded that discussion of "necessary in the public interest" (as used in Section 202(h) of the Communications Act) was *dicta* that did not reflect full consideration of the issue; indeed, as the panel noted on

in those cases use only the word "necessary"[13] and not – unlike Section 11 – the term of art "necessary in the public interest," which has been separately construed by the Supreme Court in the more applicable context of adopting and retaining rules.[14]

Contrary to Verizon's claim (at 5), this reading of "necessary in the public interest" does not render Section 11 a "toothless tiger." Section 11 requires the Commission to devote resources to re-examining its rules every two years, which invariably results in the repeal of some rules. Prior to the 1996 Act, the Commission did not undertake such reviews, and rules stayed on the books years after they had outlived their purpose or usefulness. As such, Section 11 serves the precise purpose for which it was intended: to overcome natural inertia by requiring a review every two years.

Section 11, however, has no more radical purpose. As the Commission told the D.C. Circuit, it would stand this provision on its head to read it, as Verizon seeks to, as imposing on the Commission a standard for retaining a rule that is tougher than the standard for its initial adoption.[15] Section 11 instead recognizes that there is a presumption that existing rules are lawful and in the public interest, and that rules should be repealed only when that initial public

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reconsideration, "[t]his important question was barely raised by petitioners and was not addressed at all by the Commission or the intervenors."[12] In short, the *Fox* decisions undermine, rather than support Verizon's position.

[13] *See* 47 U.S.C. § 251(d)(2)(A) (stating that Commission must consider whether access to proprietary UNEs "is necessary" before ordering access); *id.* § 251(c)(6) (requiring collocation "necessary for interconnection or access to unbundled network elements); *id.* § 253(d) (permitting the Commission to preempt state or local laws "to the extent necessary to correct such violation or inconsistency").

[14] Additionally, Verizon's simplistic claim (at 3 n.9) that "necessary" should be interpreted according to its "ordinary meaning" fails, because – aside from the fact that Verizon's ignores the rest of the phrase "necessary *in the public interest*," – the word "necessary" has multiple "ordinary meanings." *See United States* v. *Lipscomb*, 299 F.3d 303, 324 (5th Cir. 2002) (citing *M'Culloch* v. *Maryland, supra*, for the proposition that "'necessary' has a range of meanings, including 'needful, requisite, essential, or conducive to.'").

[15] *Id.* at 10.

interest test can no "no longer" be met.[16] A regulation promulgated to address market power, for example, remains "necessary in the public interest" absent compelling evidence that the relevant market power has entirely dissipated.

B. Section 11 Maintains The Burden Of Proof On The Entity Challenging A Given Regulation.

Verizon argues that the Commission must, on a rule-by-rule basis, produce "clear" and "substantial" evidence that a rule must be retained and, therefore, that the burden of proof is on those who would have the Commission retain an existing rule. In Verizon's view, the Commission must not only complete all of its existing rulemaking proceedings (including the Treinnial review of UNEs and both broadband proceedings), but also effectively to initiate and comlete a rulemaking with respect to every single other regulation it dares to retain, supported by substantial record evidence – regardless whether any party makes a compelling case that the public interest rationale for the rule "no longer" exists, or, indeed, even *identifies* the rules to which they object and why.

Verizon's reading of Section 11 as re-acquiring that every Commission rule must be formally re-adopted every two years with a new, full justification is manifest nonsense. This irrational construciton of the statute would place an impossible burden on the Commission (which is precisely why Verizon advocates it).[17] The inevitable result of Verizon's distorted

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[16] *See* 47 U.S.C. § 161(b) (requiring determination as to whether a given regulation was "*no longer* necessary in the public interest") (emphasis added).

[17] *See, e.g.*, *Gay* v. *Sullivan*, 966 F.2d 1124, 1129 (7th Cir. 1992) (stating that statute shouldn't be read to place impossible burden on Commission; rejecting interpretation of statute that would cause "the agency [to be] whipsawed"); *cf. Rector of Holy Trinity Church* v. *United States*, 143 U.S. 457 (1892) ("It is a familiar rule that a thing may be within the letter of the statute and yet not within the statute, because not within the sprit nor within the intention of its makers."); *FDIC* v. *Elefant*, 790 F.2d 661, 666 (7th Cir. 1986) ("it is almost never right to construe a statute, however 'plain,' in a way that saps the language of effect and undermines what Congress set out to achieve").

view of Section 11 would be disastrous repeals of numerous regulations that continue to serve the public interest in discouraging or facilitating the detection of market power abuses. Nothing in the statute permits – much less requires – the Commission to accept Verizon's absurd argument.[18]

C. The Claim That The Commission Must Complete Its Review Of All Of Its Regulations Within An Even-Numbered Year Is Incorrect.

Finally, there is no merit to Verizon's claim (at 7) that the Commission must finish the review and determination within the even-numbered year.[19] This can easily be demonstrated by comparing Section 11 to other provisions of the Act that do establish firm deadlines for final Commission decisions.

For example, Section 251(d) states that "*[w]ithin 6 months* after [the date of enactment of the Telecommunications Act of 1996] the Commission *shall complete all actions* necessary to establish regulations to implement the requirements of this section."[20] Similarly, the Act specifies that the Commission "*shall . . . issue* an order concluding" an investigation of a complaint after November 3, 1998, "*within 5 months* after the date on which the complaint is

[18] Indeed, Section 11 itself recognizes that the review of regulations is intimately related with the goal of competition, for Section 11 seeks determinations only with respect to rules that are no longer necessary in the public interest "as a result of meaningful competition." Indeed, this clearly suggests that a precondition to the Section 11 review is that the party challenging a given rule must demonstrate that meaningful competition now exists, making the rule no longer necessary in the public interest. A generic (and correct) finding that the Bell Operating Companies retain substantial market power is alone sufficient to demonstrate that many of the Commission's current rules remain necessary in the public interest.

[19] To the extent that Verizon is arguing that failure to complete the review and determination of a given rule during an even-numbered year means that the rule must be repealed, its interpretation conflicts with the Administrative Procedure Act, which requires that a repeal of a rule can occur only if the agency engages in a rulemaking proceeding, including notice and comment. 5 U.S.C. § 551(5); *Natural Resources Defense Council, Inc.* v. *U.S. EPA*, 703 F.2d 700, 703 (3d Cir. 1983).

[20] 47 U.S.C. § 251(d) (emphasis added). *See also id.* § 254(a)(2); *id.* § 254(g) ("Within 6 months after the date of enactment of the Telecommunications Act of 1996 . . . , the Commission shall adopt rules" regarding rates charged by IXCs in certain contexts.).

filed."[21] Section 11, by contrast, merely states that the Commission shall in each even-numbered year "review" its regulations and "determine" whether any of its regulations are "no longer necessary in the public interest" – but includes *no* language establish a deadline for the review to be completed.[22] Congress clearly knew how to set an inflexible deadline for completion of Commission action when that was appropriate – and it chose *not* to do so in Section 11.[23]

The contrast between Section 11 and Section 10 – which governs the related question of petitions for forbearance of Commission regulations – is particularly instructive. Section 10, provides that if the Commission does not act within a certain time frame, the forbearance petition is deemed granted.[24] Again, Section 11 contains no such provision specifying that failure to act has any consequence for a rule or regulation. That makes perfect sense – Section 10 is directed at petitions for forbearance from a specific regulation, rather than, as Section 11, at all regulations in the abstract. Congress knows how to make inaction have a consequence (such as granting forbearance) – and, again, it chose not to use such a mechanism in Section 11.[25]

Contrary to Verizon's claim, the plain text of Section 11 contains no requirement that the Commission complete its review within a fixed period, much less that Commission must undertake a full-blown notice-and-comment rulemaking on the retention of every single

[21] *Id.* § 208(b)(1) (emphasis added).

[22] *Id.* § 161.

[23] Even where Congress has set a definite deadline to "complete" a given task, courts have permitted the Commission to continue that task past the statutory deadline. For example, even though Congress required the Commission to "complete the proceedings" necessary to reform the Universal Service Fund ("USF") by July 1997, 47 U.S.C. § 254(a)(2), the Fifth Circuit upheld the Commission's decision instead to chart a course toward overhaul to be completed in 2000. *See Texas Office of Public Util. Counsel* v. *FCC*, 183 F.3d 393, 406 (5th Cir. 1999).

[24] 47 U.S.C. § 160(c) ("Any such petition shall be deemed granted if the Commission does not deny the petition for failure to meet the requirements for forbearance under subsection (a) of this section within one year after the Commission receives it, unless the one-year period is extended by the Commission.").

Commission rule.[26] Instead, the most natural reading of that provision is the one that the Commission has given it in practice: the Commission reviews its regulations, produces a report suggesting candidates for repeal, and it seeks comment on those rules. Parties that believe other regulations should no longer be applied are free to file Section 10 petitions with respect to any regulations that the Commission does not include in its report, and the Commission must act on those petitions. In short, as long as the Commission does an initial review of its regulations on a bi-annual basis, and then conducts a more strenuous review of the regulations that the Commission determines may no longer be "necessary in the public interest," Section 11 is satisfied.[27]

II. THE COMMISSION SHOULD NOT REPEAL EXISTING ACCOUNTING AND RECORD KEEPING RULES.

USTA's comments seek elimination of virtually *all* of the Commission's accounting and record keeping rules. But now clearly is not the time to release the incumbent LECs, which still maintain overwhelming market power, from accounting and record keeping requirements designed to detect and thwart incumbents' ability to wield that market power to the detriment of consumers and competition. Incumbent LECs still control the bottleneck local

[25] This distinction in language also demonstrates that the burden of proof under Section 11 is on the party seeking repeal, because it emphasizes that the Commission need not make a specific finding as to the current "necessity in the public interest" of a given regulation in order to maintain it for some period of time.

[26] Unlike Section 11, other provisions of the Act require the Commission to provide a written statement of reasons for its action. *See, e.g.*, 47 U.S.C. § 405 (stating that Commission, when issuing an order on reconsideration, "shall enter an order, *with a concise statement of the reasons therefor*," denying or granting, in whole or in part, the petition) (emphasis added). Again, the contrast with Section 10 is instructive. Section 10, which governs requests by entities affirmatively asking the Commission to forbear from a regulation, requires the Commission to "explain its decision [approving or denying a petition for forbearance] in writing." Section 11, however, contains no such language.

[27] Even if Verizon were correct – and the above analysis makes plain that it is not – the Commission could make a blanket determination, based on the exhaustive review that it had already undergone in adopting its rules, that all of its rules should be retained on an interim basis while it continued to examine the evidence put forward through administrative proceedings.

telecommunications facilities to which competitors require access for local competition to develop and, therefore, incumbents continue to have both the incentive and ability to deter local entry by providing competitors with discriminatory access to those facilities. Moreover, with their increasing entry into long distance markets, incumbents LECs now have greater incentives than ever to use their local bottlenecks to impede long-distance competition and to discriminate in favor of their long distance affiliates. As incumbent LECs enter long-distance markets, those carriers have the capacity to provide customers "end-to-end" service (*i.e.,* a bundle of local and long distance services). And incumbent LECs have every incentive to deter competition by charging rates for access to bottleneck local facilities that make it economically infeasible for competitors to provide competing end-to-end services, and to provide low quality service to competitors that create further impediments to competitors' ability to compete. In addition, incumbent LECs clearly retain the incentive to cross-subsidize their long-distance offerings with revenues from their local offerings.[28]

For all of these reasons, there is no possible basis to summarily gut the Commission's current accounting and record keeping safeguards – which help detect and deter incumbent LECs from acting on their strong anticompetitive incentives. On the contrary, the recent telecommunications accounting scandals, including Qwest's admissions that it has misstated earnings reports and violated Section 272 of the Communications Act, underscore that the Commission's accounting safeguard regulations remain vital to carrying out the pro-competitive policies of the 1996 Act. Now is the time for careful and measured consideration of how to

[28] The Commission has recognized that incumbent LECs continue to have substantial market power. *See, e.g.,* Report and Order, *Policy and Rules Concerning the Interstate, Interexchange Marketplace; Implementation of Section 254(g) of the Communications Act of 1934, as amended; 1998 Biennial Regulatory Review – Review of Customer Premises Equipment And Enhanced Services Unbundling Rules In the Interexchange, Exchange Access And Local Exchange Markets,* 14 FCC Rcd. 7418, ¶ 43 (2001).

make the Commission's accounting rules better; not the wholesale elimination of those safeguards as USTA proposes.

The Commission already has begun the process of carefully reviewing its existing accounting rules by establishing a Federal-State Joint Conference Board to review them.[29] The purpose of the Joint Conference is to "provide a focused means by which [the Commission] . . . and interested state commissions may conduct an open dialogue, collect and exchange information, and consider initiatives that will improve the collection of adequate truthful, and thorough accounting data for regulatory purposes."[30] And the goal of the Joint Conference is to "help restore public confidence in the telecommunications industry by improving regulatory accounting and related reporting requirements."[31] The Commission therefore has taken proper and necessary steps to ensure that its accounting safeguard rules can be fully reviewed and strengthened or streamlined where necessary. Thus, in light of the continuing necessity of the Commission's accounting safeguard rule, and the Commission's convening of a Federal-State Joint Board to review those rules, USTA's proposal immediately to eliminate virtually all of the Commission's accounting safeguards rules by implementing the myriad accounting deregulation proposals advanced in its *Phase II* and *Phase III* accounting safeguards pleadings must be rejected.

There is, of course, a separate and independent reason to reject USTA's proposals. USTA provides virtually no support – often less than a few conclusory sentences – to support its claims that entire sections of the Commission's accounting rules should be erased. USTA does

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[29] *See* Order, *Federal-State Joint Conference On Accounting Issues*, FCC 02-240, WC Docket No. 02-269 (released September 5, 2002) ("Joint Board Accounting Order").

[30] Joint Board Accounting Order ¶ 4.

[31] *Id.* ¶ 8.

not even attempt to make the required showing that the Commission's accounting regulations are "no longer necessary in the public interest as the result of meaningful economic competition between providers of such services."[32] Nor could it, as noted, incumbent LECs continue to maintain overwhelming market power over local telephone networks. There is therefore no basis in the record for the Commission to adopt any of USTA's proposals.

ARMIS Reporting. USTA's proposal to eliminate the Commission's ARMIS reporting requirements must be rejected. The sole justification offered by USTA for eliminating the ARMIS reporting requirements is that "most of the reports have outlived their usefulness."[33] That assertion is obviously wrong (not to mention completely unsupported).

ARMIS data are central to the implementation of virtually every one of the Commission's initiatives implementing the 1996 Act. As explained by the Commission, "[w]e believe that continuing to require ARMIS reports . . . is necessary to provide us with the financial and operating data [necessary] . . . to administer [the Commission's] . . . accounting, cost allocation, jurisdictional separations and access charge rules, and to preserve our ability to monitor industry developments and quantify the effects of alternative regulatory proposals."[34] Moreover, the reports are used by the Commission to compute universal service support and contribution levels,[35] and to ensure that ILECs provide sufficiently high quality services to

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[32] 47 U.S.C. § 161(b).

[33] USTA at 9.

[34] Opinion, *Implementation of the Telecommunications Act of 1996; Reform of Filing Requirements and Carrier Classifications; Anchorage Telephone Utility, Petition for Withdrawal of Cost Allocation Manual*, 12 FCC Rcd. 8071, ¶ 58 (1997).

[35] *See* Tenth Report and Order, *Federal-State Joint Board on Universal Service; Forward-Looking Mechanism for High-Cost Support For Non-Rural LECs*, 14 FCC Rcd. 20156, ¶ 346 (1999).

wholesale customers such that local and long-distance telephone competition can grow and thrive.

State regulators also rely on ARMIS data to carry out their obligations under the 1996 Act.[36] For example, the Commission has established Total Long Run Incremental Cost ("TELRIC") as a method for pricing unbundled network elements ("UNEs"). In making TELRIC pricing determinations, many states use models similar to the one the Commission uses to determine universal service support, which rely on ARMIS data.[37] Elimination of the ARMIS reports would therefore cripple state efforts to implement and enforce Section 251 of the 1996 Act at a time when such issues are becoming more important than ever.[38] As the Wyoming PSC concluded, "[t]he use of national accounting and reporting data is extensive and should not be eliminated on a casual basis or without good cause."[39]

For these reasons, it is clear that the ARMIS reporting requirements have not remotely "outlived their usefulness," but continue to be a critical component of federal and state efforts to

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[36] *See, e.g.*, Fifth Memorandum Opinion and Order, *1998 Biennial Regulatory Review – Review of ARMIS Reporting Requirements; Petition For Forbearance Of The Independent Telephone And Telecommunications Alliance*, 14 FCC Rcd 11443, 11463 (¶ 38) (1999) ("ARMIS data are relied upon by many state commissions") ("*ITT Forbearance Order*").

[37] *See, e.g.*, Notice of Proposed Rulemaking, *2000 Biennial Regulatory Review – Comprehensive Review of the Accounting Requirements and ARMIS Reporting Requirements for Incumbent Local Exchange Carriers: Phase 2 and Phase 3,* 15 FCC Rcd. 20568, ¶ 19 (2000) ("Phase 2 and Phase 3 NPRM") ("Class A accounting data may be used by the states on a comparative basis in state UNE pricing proceedings. . . . Part 32 organizes telecommunications costs in a manner that allows a logical mapping of these costs to telecommunications rate structures. Switching costs, for example, currently are tracked separately from transport costs under our Part 32 rules. This cost distinction permits the carriers' use of separate rate structures for switching and transport UNEs, thus facilitating the states' efforts to compare costs and rates for each UNE."); *see also* Wyoming PSC at 4 (explaining that ARMIS data is used to compare "quality of service [and]. . . reviewing wholesale prices and discounts that are determined under the [1996 Act].").

[38] There are numerous other examples where state commission's rely on ARMIS data. For example, some state commissions rely on those reports to determine incentives and penalties for "price regulated companies." *ITT Forbearance Order* ¶ 24 & n.56 (discussing state proceedings in which state regulators used ARMIS data), n.58 (noting that the Wisconsin Commission "state that it develops four measures for determining incentives and penalties for price regulated companies based on data from Table II of ARMIS 43-05 report for all companies nationwide").

[39] Wyoming PSC at 4.

implement the 1996 Act. And the benefits of ARMIS reporting continue to far outweigh the costs of that reporting. The systems needed to generate the ARMIS data are already established and were funded by captive ratepayers years ago.[40] The small cost of printing those reports and making them available to regulators does not even come close to outweighing the substantial benefits of that information.

Section 272 Separate Affiliate Rules. Verizon rehashes the argument it advanced in an ongoing Commission proceeding that the Commission should allow the section 272 separate affiliate requirements to sunset in their entirety. Setting aside the fact that Verizon's claim should be addressed in the proceeding where the Commission has built (and continues to build) a record on those issues, AT&T has demonstrated that Verizon's argument is fundamentally flawed.

There is no question that the section 272 safeguards should not be allowed to sunset, but should instead be extended to all BOCs, for at least another three years. It is indisputable that, even where the BOCs have been approved under section 271 and been found to have opened their markets to competition, local markets are nowhere near the robust competition that Congress intended and that is necessary to dissipate BOC local market power. To the contrary, development of local competition even in large states has been "anemic," and, as the Chairman recently acknowledged, has occurred at a much slower pace than the Commission expected. Even in New York, the first state in which a BOC received section 271 approval and one of the states most attractive to local competitors, state regulators have found that years after section 271 approval, the BOC there "continues to dominate the market" for key services and still controls

[40] *See* Reply Comments of AT&T, *2000 Biennial Review – Comprehensive Review of the Accounting Requirements and ARMIS Reporting Requirements for Incumbent Local Exchange Carriers: Phase 2 and Phase 3*, CC Docket

bottleneck facilities upon which its rivals remain dependent.[41] And in Texas, the second state receiving section 271 authority, the Public Utility Commission of Texas has supported extension of the section 272 safeguards because of, among other reasons, the "lack of alternative access points to [BOC] network."[42] Under these market conditions, it would be unthinkable for the Commission – alone among lawmakers and regulators – to determine that structural, transactional, and nondiscrimination safeguards should be *removed*, rather than strengthened and more vigorously enforced.

As demonstrated by AT&T, the BOCs' own conduct provides the best demonstration of their enduring market power and the immediate need for increased attention to and continued application and enforcement of section 272 safeguards.[43] The BOCs have consistently engaged – and continue to engage, even in states in which they have obtained section 271 authority years ago – in the very types of misconduct that Congress expected would occur in the period after section 271 authority is granted but before full competition developed to constrain local market power. The evidence AT&T has compiled – which includes findings from regulators and independent auditors – shows, for example, that BOCs provide the special access services that are a key input into long distance services in a discriminatory manner that treats the BOCs' rivals less favorably than the BOCs' retail customers. And BOCs have also been found to inflict harm on the long distance market by implementing PIC changes and PIC freezes – the processes by

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No. 00-199, at 3 (filed March 14, 2001) (describing USTA, Verizon and Qwest admissions that they maintain systems that track the ARMIS information).

[41] *See Opinion and Order Modifying Special Services Guidelines for Verizon New York Inc., Conforming* Tariff*, and Requiring Additional Performance Reporting*, Case 00-C-2051, (NYPSC June 15, 2001).

[42] *See* Comments of Texas Office of Public Utility Counsel, WC Docket No. 01-148 (filed July 17, 2002) (quoting Report to the 77th Texas Legislature, *Scope of Competition in Telecommunications Markets of Texas*, January 2001, p. ix-x).

[43] *See* Comments of AT&T Corp., *Section 272(f)(1) Sunset of the BOC Separate Affiliate and Related Requirements*, WC Docket No. 02-112 (filed August 5, 2002).

which long distance carriers win and retain their customers – in a discriminatory fashion. These findings confirm the BOCs' enduring local market power and also demonstrate that section 272 safeguards remain critical for competitors and regulators to detect and measure the BOC misconduct in the first instance.

The BOCs also continue to engage in pervasive and improper cost misallocation, which aids the BOCs' long distance affiliates and harms their unaffiliated rivals. In Texas, for example, SBC is failing to impute access charges to itself, and is offering through its affiliate long distance services at rates that are nearly equal to the BOC's intrastate access charges. This is a classic price squeeze that again demonstrates the BOCs' continued market power and the need for enforcement of section 272 safeguards to detect and remedy such conduct. Additionally, BOC long distance affiliates are receiving huge anticompetitive advantages through the receipt of BOC marketing services and assets at extremely low prices that clearly demonstrate cross-subsidization.

Such conduct would be almost impossible to police if section 272 accounting and structural safeguards were not in place. Thus, both theory and marketplace evidence compel the conclusion that the Commission should promulgate a blanket continuation of all section 272 safeguards for at least three years, and provide an ample basis for the Commission to reject any of the less robust alternatives proposed in the *Notice.* On this record, Verizon's proposal to simply declare in the biennial review process that section 271 requirements will sunset must be rejected.

In the alternative, Verizon's and USTA's claim that the Commission should eliminate its rules that prohibit the sharing of operating, installation and maintenance ("OI&M") functions between a BOC and its Section 271 affiliate should be rejected.[44] In the *Non-Accounting Safeguards Order*, the Commission concluded "that allowing the same personnel to perform the operation, installation, and maintenance services associated with a BOC's network and the facilities that a section 272 affiliate owns or leases from a provider other than the BOC would create the opportunity for such substantial integration of operating functions as to preclude independent operation, in violation of section 272(b)(1)."[45] Relying on a principle established in 1983 when the BOCs were first created, the Commission stressed that section 272(b)(1)'s "operate independently" requirement barred such sharing of operation, installation, and maintenance services, in part because such shared service arrangements "would inevitably afford access to the BOC's facilities that is superior to that grant to the affiliate's competitors," and "would create substantial opportunities for improper cost allocation."[46] The OI&M prohibition therefore is a vital tool to fulfilling section 272's central purpose of "prohibit[ing] anticompetitive discrimination and cost-shifting."[47]

The BOC's strongly objected to the Commission's OI&M safeguard and sought reconsideration. The Commission rejected these reconsideration requests, reaffirming that section 272 precludes shared OI&M services, and recognizing that any other ruling would "create a loophole around the separate affiliate requirement" and would provide for such "substantial integration of these essential functions . . . that independent operation would be

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[44] USTA at 14; Verizon at 12-14. Notably, these claims are the subject matter of another rulemaking proceeding that currently is pending before the Commission. Public Notice, *Wireline Competition Bureau Seeks Comment On Verizon's Petition For Forbearance From The Prohibition Of Sharing Operating, Installation And Maintenance Functions*, CC Docket 96-149 (released Aug. 9, 2002).

[45] *Non-Accounting Safeguards Order* ¶ 163.

[46] *Id*.

[47] *Id.* ¶ 9; *see* 47 U.S.C. § 272(b) (establishing the "operate independently," "arm's length" dealing, and other accounting safeguards on the section 272 affiliate); *id.* § 272(c) (imposing broad and unqualified prohibitions against discrimination by the BOC).

precluded."[48] Verizon's and USTA's arguments in this proceeding rehash (in summary form) the same arguments that the Commission has repeatedly rejected. And neither Verizon nor USTA point to any changed circumstances that could provide any reasonable basis for the Commission to change course and decide that the OI&M services restriction is no longer required by Section 272 and no longer is necessary to protect competition, consumers, and the public interest.[49]

Indeed, Verizon's and USTA's claims that the Commission's concerns of improper cost allocation are misplaced, and that the OI&M services restriction results in a loss in efficiency and fewer new services are the precise arguments previously presented by the BOCs and rejected by the Commission.[50] And Verizon's claim that "new" information concerning the costs of the OI&M restriction, which the Commission did not have when it first announced the rule, justifies this result, cannot be credited. The conclusory claims of its costs of compliance with the OI&M services restriction are unsupported and unaccompanied by any documentation that could allow them to be independently verified.[51]

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[48] *Non Accounting Safeguards Third Order on Reconsideration*, 1999 WL 781649, 17 Comm. Reg (P&F) 920, ¶ 20 (1999).

[49] As noted, the underlying basis for the OI&M rule, and for the operate independently and nondiscrimination requirements – the BOC's market power in the local exchange market and its ability and incentive to leverage this market power to undermine competition in the long distance market – is as strong now as it was when the Commission first announced the rule. *See, e.g., See* AT&T's Opposition To Verizon Petition For Forbearance, *Petition of Verizon for Forbearance From The Prohibition of Sharing Operating, Installation, and Maintenance Functions Under Section 53.203(a)(2) Of The Commission's Rules*, CC Docket No. 96-149, at 6 (filed September 9, 2002) ("AT&T OI&M Comments").

[50] *See*, *e.g.*, *Non-Accounting Safeguards Order*, ¶¶ 153, 163 (rejecting BOCs' claim that OI&M restriction is inappropriate because it will "result in a loss of efficiency and economies of scope, decreased innovation, and fewer new services"). The Commission again rejected these claims in the *Non-Accounting Safeguards Second Order on Reconsideration*, 12 FCC Rcd. 8653, ¶¶ 11-12 (1997), and in the *Non-Accounting Safeguards Third Order on Reconsideration*, 17 Comm. Reg (P&F) 920 (1999).

[51] In fact, if there was any error in the Commission's original balancing of costs and benefits in this area, it is that the Commission *underestimated* the competitive harm arising from shared BOC/272 affiliate services, and allowed *too much* sharing and too many opportunities for anticompetitive cost misallocations and discrimination. Verizon and other BOCs have clearly exploited these opportunities. Indeed, recent 272 audits have revealed pervasive

Nor can there be any serious claim that the OI&M safeguard seriously handicaps the BOCs. Verizon, for example, claims that its 272 affiliate, with only 800 employees, has quickly gained up to 34.2% market share, more than other facilities-based and better-staffed competitors gained in many years.[52] The relatively small costs of the prohibition against joint OI&M remain critically necessary and clearly impose no serious or unwarranted restriction on Verizon, given that it has already become one of the largest long distance carriers in the nation with the OI&M safeguards in place.

Record Preservation. The Commission's Part 42 rules require incumbent LECs to maintain and preserve certain records, and to make those records available to the Commission upon request.[53] Those requirements are necessary to allow the Commission to ensure that incumbent LECs – which continue to wield overwhelming market power – are complying with the Commission's rules and the 1996 Act, and to allow the Commission to investigate allegations of incumbent LEC misconduct. USTA, however, urges the Commission to eliminate those rules on the sole unsupported grounds that those regulations are "outdated and unnecessary."[54]

Predictably, USTA provides no supporting documentation or other evidence to support its claims that the Commission document preservation rules are outdated and unnecessary. Nor

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violations of the sharing and other 272 rules that do exist. AT&T OI&M Comments at 3-4. State commissions and competing carriers have likewise compiled a substantial record in the section 272 sunset proceeding showing that BOCs retain market power, even in states where they have long been offering long distance service – including in several non-BOC territories where section 271 authorization was not even required. As a result, there is still a substantial risk of discrimination and cost misallocation by the BOCs – the very conduct that the Commission has for years determined the OI&M prohibition is absolutely necessary to prevent. Given the substantial threat that BOCs can leverage local market power to re-monopolize the long distance market, the OI&M ban should be retained.

[52] AT&T OI&M Comments at 4.

[53] *See* 47 C.F.R. Part 42.

[54] USTA at 8.

could it. As noted, those rules continue to be critical to allowing the Commission to effectively regulate and investigate incumbent LECs that are subject to federal regulation, because they continue to have substantial market power. Thus, USTAs proposal to eliminate Commission Part 42 must be denied.

Cost Allocation Manual. USTA urges the Commission to eliminate cost allocation manual filings for even the largest incumbent LECs. Again, the Commission recently has rejected that argument, noting that those rules "are increasingly important as more carriers diversify into competitive ventures,"[55] and USTA has offered no new evidence to support its claim that the Commission should reverse its prior actions. Accordingly, the Commission should reject this request.

International Data Reports. The Commission's accounting rules and policies continue to play a vital and necessary role in international markets as well. Monopoly foreign carriers (often government-owned) still control the foreign end on three out of four U.S. international routes,[56] and U.S. carriers continue to pay above-cost termination rates in most countries.[57] Consequently, U.S. consumers still pay hundreds of millions of dollars in above-cost subsidies to foreign carriers through artificially high prices, and foreign carriers can still use above-cost termination rates to harm U.S. competition.[58]

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[55] *See* Report and Order in CC Docket Nos. 00-199, 97-212, 80-286, 99-301, Report and Order in CC Docket Nos. 00-199, 97-212, 80-286, and Further Notice of Proposed Rulemaking in CC Docket Nos. 00-199, 97-212, 80-286, *2000 Biennial Regulatory Review – Comprehensive Review of the Accounting Requirements and ARMIS Reporting Requirements for Incumbent Local Exchange Carriers; Phase 2 Amendments to the Uniform System of Accounts for Interconnection Jurisdictional Separations Reform and Referral to the Federal-State Joint Board Local Competition and Broadband Reporting*, 16 FCC Rcd. 19911, ¶ 192 (2001)

[56] U.S. carriers provide services on more than two hundred international routes, but only fifty countries have international telephone service competition. *See TeleGeography 2002*, Fig. 3.

[57] *See, e.g., International Settlements Policy Reform*, IB Docket No. 02-324, Notice of Proposed Rulemaking, FCC 02-285 (rel. Oct. 11, 2002), ¶ 44 ("benchmark rates are still considerably above actual cost-based rates."). *See also, e.g., AT&T and Concert Objection to International Settlements Policy Modification Request for a Change in the Accounting Rate for International Message Telephone Service with Mexico*, IB Dkt. ARC-MOD-20010530-00123, Jun. 20, 2001, Atts. A&B (termination costs in Mexico are under 4 cents).

[58] Report and Order, *International Settlement Rates*, 12 FCC Rcd. 19806, ¶ 2 (1997).

Section 43.61, 43.82 and 63.10 reporting requirements allow effective enforcement of Commission policies promoting competition and protecting against competitive harm in the U.S. international market. Verizon contends that (at 9-10) the Commission should "eliminate" all these reports on the (incorrect) ground that these reports "do not serve" their "stated purpose" of monitoring compliance with settlement rate benchmarks. Verizon is wrong. The information provided by these reports not only serves that important purpose, but also is necessary for effective enforcement of other pro-competitive Commission international rules and policies in furtherance of the public interest.

Notwithstanding Verizon's assertions to the contrary, an important function of Section 43.61 reports is to assist the effective enforcement of Commission rules and policies encouraging lower foreign termination rates. Those reports, which include details of U.S. outbound and inbound international traffic volumes and revenues on a route and service-specific basis, allow the Commission to monitor foreign termination rates, and facilitate the progress achieved by the Commission's benchmarks and International Settlements Policy in reducing those rates toward cost-based levels. Section 43.61 reports also allow the Commission to monitor U.S. outpayments to different countries, inbound and outbound traffic streams, shifts in traffic among different services, and other changes resulting from increasing competition. And the reports facilitate the detection of anticompetitive conduct by foreign carriers that may adversely affect the U.S. market, such as one-way by-pass and price squeeze behavior.[59] These many public interest benefits greatly outweigh the costs of producing Section 43.61 traffic and revenue data,

[59] *Id*. ¶¶ 219, 242. Verizon wrongly claims (at 10) that these reports do not distinguish between "non-settled" and "settled" traffic, which is reported in different categories. *See id*. ¶ 252.

and any concern about revealing competitively-sensitive information may be addressed by filing on a confidential basis.

Similarly, the quarterly Section 43.61 reporting requirement, which Verizon also seeks to remove, was established by the *Benchmarks Order* as an additional safeguard specifically to allow the rapid detection of U.S. market distortion resulting from foreign carrier one-way by-pass and price-squeeze activity.[60]

Verizon also offers no legitimate explanation for its proposal to eliminate Section 63.10 dominant carrier and Section 43.82 international circuit status reports in its broad-brush request. Section 63.10(c) requires dominant carriers to file quarterly traffic and revenue reports, quarterly circuit status reports, and quarterly reports summarizing the provisioning and maintenance of facilities and services procured from its foreign affiliate. All of this information is critical to preventing carriers with foreign market power from harming U.S. competition.[61] Section 43.82 annual circuit status reports facilitate Commission efforts to achieve a more competitive international market by providing information not available from other reliable sources to assist market entry and expansion decisions.[62] Because Verizon provides no legitimate evidence to show why these reports are no longer important to encourage further competition in the U.S. international services market, Verizon's proposal to eliminate those rules must be rejected

[60] *Id.* ¶¶ 224, 226, 248.

[61] Report and Order and Order on Reconsideration, *Foreign Participation in the U.S. Telecommunications Market*, 12 FCC Rcd. 23891, 23897, 24013-24020 ("Foreign Participation Order") (1997).

[62] Report and Order, *Rules for the Filing of International Circuit Status Reports*, 10 FCC Rcd. 8605, ¶ 5 (1995).

III. THE COMMISSION SHOULD REJECT THE PROPOSED CHANGES TO THE UNIVERSAL SERVICE MECHANISM.

USTA and NTCA propose certain changes to the universal service system, including adding equal access to the definition of universal service and making other changes to the rural health care support mechanism. Neither change should be adopted.

Equal Access. USTA and NTCA argue that the Commission should add equal access to the definition of universal service.[63] Such a request is inappropriate in the context of a Section 11 biennial review. Adding services to the definition of universal service would constitute an *expansion* of the universal service system, not repeal or modification, and could only be accomplished through an affirmative rulemaking after referral to the Federal-State Joint Board on Universal Service.[64] As USTA concedes, the Joint Board issued a Recommended Decision addressing these issues on July 10, 2002, and the Commission has not yet sought comment on the Joint Board's recommendations.[65] Any further consideration of these issues could only take place within the existing universal service docket, and not in the context of this biennial review.

In all events, the Commission should not add equal access to the definition of universal service. Equal access is not "essential to education, public health, or public safety," as required by Section 254(c). Access to interexchange service is already included in the definition of universal service, and therefore "[c]onsumers can call community service organizations located outside of the calling area without equal access."[66] While the availability of equal access is an

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[63] *See* USTA at 15; NTCA at 5-6.

[64] *See* 47 U.S.C. 254(c).

[65] *See Federal-State Joint Board on Universal Service*, CC Docket No. 96-45, Recommended Decision (released July 10, 2002) ("*Recommended Decision*").

[66] *Recommended Decision* ¶ 73.

important prerequisite to a competitive interexchange market, "the absence of an equal access requirement for all [eligible telecommunications carriers] does not impair universal service."[67]

Rural Health Care Mechanism. NTCA also seeks certain changes to the Rural Health Care Support Mechanism that would have the effect of increasing the Universal Service Fund ("USF").[68] The Commission should *not* be entertaining any changes to the universal service fund ("USF") that would trigger increased funding requirements at a time when there is tremendous instability of the fund. Wireline interstate telecommunications revenues have begun to shrink dramatically over the past couple of years, while universal service funding has increased and the USF contribution factor has swelled to its highest level ever. The revenue assessment base will continue to decline, driven by the substitution of wireless for wireline long distance, the growth of non-telecommunications long distance substitutes such as e-mail and instant messaging, and the "leakage" created as higher and higher contribution factors induce customers and their providers to structure contracts that bundle interstate telecommunications services with intrastate services, information services, and customer premises equipment to minimize the revenue attributed to interstate telecommunications services. As a result, the USF is in a "death spiral" that pushes revenues out of the assessment base, and results in ever increasing USF recovery line items for consumers.[69] Indeed, the Commission just recently adopted an order to "stabilize" the USF contribution factor for the next two to three quarters while it completes a pending proceeding to reform the entire system. The FCC indicated that it

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[67] *Id.*

[68] *See* NTCA at 9-10.

[69] *See generally* CoSUS Comments, filed April 22, 2002, CC Docket Nos. 96-45, *et al.*

expects to implement such reforms no later than April 1, 2003.[70] Having taken action to ameliorate the level of the USF contribution factor pending USF reform, the Commission should *not* take any additional actions that would increase the funding requirements.

IV. THERE IS NO BASIS FOR ADDITIONAL DEREGULATION OF ACCESS SERVICES BECAUSE THE INCUMBENTS RETAIN OVERWHELMING MARKET POWER.

The Commission should also reject the commenters' various proposals related to access charges. The ILECs retain overwhelming market power in their local exchange markets, and the commenters' proposals would repeal rules that remain vitally necessary to contain the ILECs' market power. Indeed, as AT&T has shown in its recent petition for rulemaking, the Commission should tighten regulation of special access charges; it certainly should not repeal the dwindling number of regulatory safeguards that remain.

All-Or-Nothing Rule. USTA and CenturyTel argues that the Commission should repeal the "all-or-nothing" rule, which requires a rate-of-return company to convert to price caps if it acquires an exchange governed by price caps.[71] As CenturyTel notes, this issue has been raised and fully briefed in the MAG proceeding. And as AT&T there explained, the Commission should *enforce* the all-or-nothing rule, not repeal it.

The all-or-nothing rule is still necessary to guard against improper cost-shifting. As the D.C. Circuit explained in 1993, "it seems quite obvious that dual regulation . . . has a key feature in common with regulated-unregulated dual status: a firm can escape the burden of costs incurred in its unregulated *or* price cap business by shifting them to the rate-of-return affiliate,

[70] *See Schools and Libraries Universal Support Mechanism*, CC Docket No. 02-6, First Report and Order, FCC 02-175, ¶¶ 1, 3 (released June 13, 2002).

[71] *See* 47 C.F.R. § 61.41(b), (c)(2); USTA at 18; CenturyTel at 2-7.

which can pass them on to ratepayers."[72] The Court went on to affirm the Commission's "all-or-nothing" rule, which was designed to guard against such anticompetitive behavior by prohibiting LECs from owning facilities that are not subject to the same type of rate regulation. *See id*. at 181.

LECs continue to have substantial incentives to engage in price-inflating cost-shifting between incentive regulation affiliates and rate-of-return affiliates. By shifting costs from price cap affiliates to rate-of-return affiliates, LECs can increase profit margins for incentive regulation affiliates, while continuing to receive the same return for rate-of-return affiliates. In addition, LECs would have incentives to "game" the system through sequential mergers and acquisitions.[73]

The competitive concerns associated with eliminating the all-or-nothing rules are not speculative. As explained by this Commission when it first adopted the all-or-nothing rule, "the record in this proceeding, like the records developed in other proceedings before the Commission, demonstrates that LEC holding companies have both the means and the motive to shift costs improperly from affiliates under one regulatory system to affiliates under another system, to the detriment of ratepayers."[74] LECs continue to have substantial incentives to engage in improper cost shifting and continue to have the means to implement such strategies. And given the size and complex ownership structures of today's LECs, it would be virtually impossible to detect this type of anticompetitive behavior without additional (and cumbersome)

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[72] *See NRTA* v. *FCC,* 988 F.2d 174, 179-180 (D.C. Cir. 1993) (emphasis in original).

[73] *See, e.g., NRTA,* 988 F.2d at 179 ("successive mergers or acquisitions [that] enabled a firm to shift back and forth between rate-of-return and price cap [would create] . . . a risk of sequential cost shifting").

[74] *Policy and Rules Concerning Rates for Dominant Carriers*, Second Report and Order, 5 FCC Rcd. 6786, ¶ 271 (1990) ("*LEC Price Cap Order*").

accounting guidelines that would allow the Commission and interested parties to monitor LEC accounts for cost-shifting.

Indeed, the Commission's jurisdictional accounting regulations clearly are insufficient to monitor and protect against the unlawful cost-shifting and gaming strategies that dual regulation LECs would be motivated to implement. When the Commission previously addressed this same issue in 1990, it explained that "[w]hile state regulation may be adequate to detect and prevent improper inter-affiliate and intra-affiliate cost shifts from the interstate category to the intrastate category, it is neither designed nor able to detect such cost shifts within the interstate jurisdiction."[75] The D.C. Circuit agreed with that assessment, noting that such jurisdictional separation rules are "of little relevance for cost shifting entirely within the federal domain."[76] In addition, the Commission has noted that it did "not wish to create new administrative burdens for the Commission associated with monitoring affiliate transactions and taking appropriate enforcement action if necessary."[77] And in any event, "[s]tructural separation does not cure incentives to shift costs; it only makes cost shifting [more] detectable."[78] Thus, any claims that existing or new accounting separation rules could be used (or adopted) to avoid anticompetitive behavior by LECs that operate under dual regulation should be rejected.

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[75] *LEC Price Cap Order* ¶ 274.

[76] *See NRTA,* 988 F.2d at 180.

[77] *See ALLTEL Corporation; Petition for Waiver of Section 61.41 of the Commission's Rules and Applications for Transfer of Control,* Memorandum Opinion and Order, 14 FCC Rcd. 14191, ¶ 38 (1999) ("*ALLTEL Waiver Order*").

[78] *Id.*

Finally, LEC claims that past approval of waiver applications suggests that the Commission's all-or-nothing rules are obsolete are specious.[79] Indeed, rather than repealing the rule, the Commission should fully enforce it. The Commission's waivers in the context of mergers have allowed numerous rate-of-return carriers to remain under rate-of-return regulation, which has undoubtedly cost consumers millions of dollars in lost access charge reductions. These larger rate-of-return LECs that have been parties to these mergers are of sufficient scale to respond effectively to incentive regulation, and it is no longer in the public interest to shelter these LECs from full application of the all-or-nothing rule.

USTA Proposals. USTA argues (at 18) that all ILECs should be permitted to file contract-based tariffs, which would essentially be the equivalent of Phase I pricing flexibility. As AT&T has shown elsewhere, such pricing flexibility would be grossly premature at this time. Rate-of-return carriers already have substantial pricing flexibility that is fully sufficient. Rate-of-return carriers are already permitted to deaverage transport and special access rates in a study area if there is a single cross-connect in that study area, and they may offer volume and term discounts on transport services if a minimum threshold of DS1s are provided in central offices in a study area. Moreover, the Commission has amended its rules to permit rate-of-return carriers to geographically deaverage their SLC rates, and the Commission has also dramatically streamlined the requirements for introducing new services.[80]

Any additional pricing flexibility would be grossly premature. Rate-of-return carriers are dominant carriers with market power, and therefore additional pricing flexibility would be

[79] *See Multi-Association Group (MAG) Plan for Regulation of Interstate Services of Non-Price Cap Incumbent Local Exchange Carriers and Interexchange Carriers, et al.,* CC Docket Nos. 00-256, Further Notice of Proposed Rulemaking, ¶ 270 (released November 8, 2001) ("*MAG Notice*").

[80] *See MAG Notice*, Comments of AT&T at 19 (filed Feb. 14, 2002).

anticompetitive unless there has been significant competitive entry. There has been virtually no competitive entry, however, in the rate-of-return LECs' territories.[81] Absent competitive entry, pricing flexibility can be "used to erect a barrier to competitive entry."[82] In particular, rate-of-return LECs could use contract tariffs to deaverage their rates to target attractive customers through lower rates or lengthy term contracts, and the LECs could fund such tactics by raising rates excessively to other customers.[83] For the foreseeable future, pricing flexibility would "inhibit competitive entry and deny customers . . . the benefits of competition."[84] Indeed, if anything, the Commission's experience with pricing flexibility for price cap carriers has demonstrated that such relief has been premature even for those carriers.[85]

USTA's comments also contain a grocery list of additional one-sentence access-related proposals, including (1) modifying Rules 65.700 and 65.702 to require calculation of rates-of-return on an aggregate, rather than targeted basis (USTA at 28) and (2) restructuring Parts 61 and 69 so that they apply only to rate-of-return carriers and creating a new Part for price cap carriers (USTA at 18, 29). USTA offers no argument or evidence in support of these various proposals and they should be rejected.

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[81] *See, e.g., Communications Daily*, p. 11 (November 14, 2001) (new Yankee Group study shows that rural LECs face little competition). The study shows that "lack of competition allows rural ILECs to control the 'customer relationship for most telecom products and services,'" and that when "the local phone monopoly segment of overall business was broken out, operating margins were 33% -- very high for telecom service provider[s]." *Communications Daily*, p. 11 (November 14, 2001). The "[m]argins for all services and products sold by rural ILECs were 16%." *Id.*

[82] *MAG Notice* ¶ 250.

[83] *Id.*

[84] *Id.*

[85] *See In the Matter of AT&T Corp. Petition for Rulemaking to Reform Regulation of Incumbent Local Exchange Carrier Rates for Intersate Special Access Services*, RM No. 10593, Petition of AT&T Corp. (filed October 15, 2002).

SLCs On T1s. Consideration of NECA's request that the Commission amend Rule 69.104 to "permit the application of no more than five SLCs . . . to customer-ordered exchange access service that is provisioned using digital, high-capacity T1 interfaces . . . for which the customer supplies the terminating channelization equipment" is inappropriate in the context of a biennial review. NECA's request is in effect a request for a ratemaking, not a repeal or streamlining. NECA itself has effectively acknowledged this in that it has already made its request in a petition for an affirmative rulemaking.[86] The Commission has not even sought comment on the petition as yet, and therefore action on NECA's request would be wholly inappropriate.

Cash Working Capital. The Commission should also reject NECA's request that the Commission extend the standard allowance period for calculating the cash working capital (CWC) element from 15 days to 30-45 days.[87] CWC is the amount of investor-supplied funds required to pay operating expenses incurred in providing services prior to the receipt of revenues for such services. CWC is generally computed by determining the revenue lag and the expense lag and then multiplying the difference by the carrier's average daily operating expenses.[88] In prior tariff proceedings, the Commission has consistently found lead-lag times in excess of 15 days to be unjustified.[89] NECA has provided no new information that would support a longer lag time, and its request should be rejected.

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[86] *See* NECA at 16.

[87] NECA at 18-19.

[88] Revenue lag is the average number of days between the date a service is provided and the date the associated revenues are collected. Expense lag is the average number of days between the date a service is provisioned and the date the expenses associated with those services are paid. The difference between revenue lag and expense lag is referred to as the net lag.

[89] *See, e.g., 1997 Annual Access Tariff Filings*, Memorandum Opinion and Order, CC Docket 97-149, ¶ 67 (1997).

V. THE COMMISSION SHOULD RETAIN THE OTHER REGULATIONS THAT ARE NECESSARY TO PROTECT CONSUMERS AND COMPETITION.

Finally, some commenters urge the Commission to eliminate or modify a smattering of regulations that have recently been upheld by the Commission. Because these commenters are unable to identify any circumstances that have changed since the Commission last rejected proposals to eliminate those rules, the Commission should decline the carriers' invitation to reverse those prior holdings.

Bundling of Enhanced Services. USTA urges the Commission to eliminate Part 64, Subpart G of the Commission's rules in order to "eliminate[] the prohibition on bundling enhanced services" for BOCs.[90] USTA's proposal must be rejected, because Part 64, Subpart G of the Commission's rules – the regulation that USTA seeks repealed – does not "prohibit" BOCs from bundling enhanced services. Rather Part 64, subpart G requires only that BOCs also provide the underlying basic service as a separate tariffed service. As explained by the Commission, the current rules "allow . . . BOCs to integrate their enhanced and basic service operations, [subject to] . . . the requirement that [BOCs] acquire transmission capacity under the same tariffed terms and conditions as competitive enhanced service providers."[91] Because USTA fails to identify a valid reason why the Commission should eliminate Part 64, Subpart G of the Commission's rules, its proposal must be rejected.

In any event, there is no legitimate basis on which USTA could seek a repeal of Part 64, Subpart G of the Commission's rules. As the Commission has found, the requirement that BOCs

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[90] USTA at 23.

[91] *See* Report and Order, *Policy and Rules Concerning the Interstate, Interexchange Marketplace; Implementation of Section 254(g) of the Communications Act of 1934, as amended; 1998 Biennial Regulatory Review – Review of Customer Premises Equipment And Enhanced Services Unbundling Rules In the Interexchange, Exchange Access And Local Exchange Markets,* 14 FCC Rcd. 7418, ¶ 43 (2001).

make the transmission facilities used to provide bundled enhanced services available to competitors on a non-discriminatory basis is essential because "the separate availability of the transmission service is fundamental to ensuring that dominant carriers cannot discriminate against customers who do not purchase all the components of the bundle from the carriers themselves."[92] Thus, there is no valid justification for USTA's proposal to eliminate Part 64, subpart G of the Commission's rules.

Pole Attachment Rules. USTA also asks the Commission to reconsider the exact same arguments advanced by USTA in the 2000 Biennial Review to further streamline the Commission's Pole Attachment Complaint procedures.[93] USTA requests that the Commission yet again reconsider USTA's argument that the average number of pole attachers should no longer be based on the average number of attachers per pole in three demographic zones. USTA does not offer any new arguments, but instead relies on the argument it advanced in 1998 – that the existing method for computing the average number of pole attachers is overly burdensome. The Commission however already has rejected that argument, concluding that "[o]ur decision that the utility would establish an average number of attaching entities was premised on the belief that utilities not only possess information with which to develop an average number of attaching entities, but also have both the expertise to structure the development of an average and the information reflecting where services are to be provided."[94] Because USTA has provided no

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[92] *See id.* ¶ 44.

[93] USTA at 5.

[94] *Amendment of the Commission's Rules and Policies Governing Pole Attachments; Implementation of Section 703(e) of the Telecommunicaitons Act of 1996*, CS Docket No. 97-98 and 97-151, Consolidated Partial Order on Reconsideration, ¶ 62-63 (2001) ("*Pole Attachment Recon. Order*"). The Commission further concluded that the three categories to be used in the average "would equitably reflect the different levels of attachment usage based on characteristics of the locations." *Id.*

additional evidence to support its proposed rule change, the Commission should again reject that proposal.[95]

LNP Cost Recovery Rules. The Commission's rules allow carriers to recover the costs of implementing local number portability ("LNP") from end users. In 1998, the Commission adopted rules that allow carriers to recover LNP costs from end users located in the 100 largest Metropolitan Statistical Areas ("MSAs"), and from end users located outside of the 100 largest MSAs that are served by an LNP-capable switch.[96] In 2002, the Commission amended those rules to allow recovery of LNP costs for carriers outside the 100 largest MSAs that do not have an LNP capable switch if the carrier participates in an extended area service calling plan with one of the 100 largest MSAs or other adjacent areas served by a number portability capable switch.[97]

NECA was disappointed with the Commission's 2002 order because, according to NECA, the order still does not permit certain carriers to recover LNP costs. NECA therefore filed a petition with the Commission seeking reconsideration of that order.[98] The comments of USTA, NTCA and NECA urge the Commission to now circumvent the reconsideration process and immediately in this proceeding modify its LNP recovery rules based on NECA's petition for reconsideration. That argument must be rejected for multiple reasons.

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[95] USTA also renews its general objection to the Commission's methodology for computing pole attachment rates, and seeks to have the Commission alter the burden of proof in complaint proceedings. These claims, however, like many of USTA's other claims, are not appropriately addressed in the biennial review process, because USTA's claims seek new rules, and not the elimination or modification of *existing* rules that are "no longer necessary in the public interest as the result of meaningful economic competition." 47 U.S.C. § 161. In any event, the Commission rejected these same claims in a recent order (*Pole Attachments Recon. Order* ¶¶ 11-42), and USTA has offered no changed circumstances to warrant reconsideration of that decision.

[96] Third Report and Order, *Telephone Number Portability*, 13 FCC Rcd 11701, ¶ 135 (1998).

[97] *See* Memorandum Opinion And Order On Reconsideration And Order On Application For Review, *Telephone Number Portability*, CC Docket No. 95-116, FCC 01-16 (released February 15, 2002) ("*LNP Recon Order*").

First, the Commission need not, and should not, short-cut its extensive rulemaking processes by granting the relief sought in petitions for reconsideration. Second, the Commission has already satisfied the biennial review obligation to review the LNP rules – the Commission reviewed those rules and issued an order earlier this year. Third, NECA's petition for reconsideration is meritless and should be rejected, because it simply rehashes the same arguments that the Commission rejected in its 2002 decision.[99] Thus, the Commission can and should reject the proposals to change its LNP rules.

Per Subscriber Listing Charge. The 1996 Act requires that telecommunications carriers provide subscriber list information to requesting directory publishers "under . . . reasonable rates."[100] In 1999, the Commission determined that "[a]fter reviewing the language of section 222(e), its legislative history, the broader statutory scheme, and Congress' policy objectives . . . [a] $0.04 per listing [charge] is a presumptively reasonable rate for base file subscriber list information."[101] Although a rate at or below $0.04 is presumptively valid, a carrier can charge a higher rate if the carrier "provide[s] cost data and all other relevant information justifying the higher rate."[102]

NECA urges the Commission to increase that the per subscriber listing charge from $0.04 to $0.42 – a ten-fold increase. The Commission should reject NECA's proposal to transform the

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[98] *See NECA Petition for Reconsideration,* CC Docket No. 95-116 (filed July 15, 2002).

[99] *LNP Recon Order* ¶ 54 ("[w]e decline to allow the non-number portability-capable LECs to recover their eligible number portability costs in access charges . . . because recovery through access charges would not be competitively neutral.").

[100] 47 U.S.C. § 222(e).

[101] Third Report and Order in CC Docket No. 96-115, Second Order on Reconsideration of the Second Report And Order in CC Docket No. 96-88, and Notice of Proposed Rulemaking in CC Docket No. 99-273, FCC 99-227, at 100 (released September 9, 1999).

[102] *Id.*

biennial review process into a ratemaking proceeding. The purpose of the biennial review process is to identify existing regulations that should be modified or eliminated, not to re-assess rates. That fact is especially relevant here, where the Commission's rules still allow carrier to charge rates higher than $0.04 if the carrier provides sufficient data to support the higher rates.

In any event, there is no legitimate basis for NECA's proposed ten-fold increase in the per subscriber listing rates. NECA's proposed rate of $0.42 is based on a survey of only "small and rural telephone" companies, and therefore excludes the much lower costs incurred by medium and large carriers.[103] That means that NECA's proposed "presumptively valid" rate is based on the highest cost telephone carriers in the country. Implementing such a high "presumptively valid rate" would provide a windfall to the much lower cost medium and large telephone carriers at the expense of ratepayers. The Commission's current rule is far better. The "presumptively valid rate" reflects the costs of the average carrier, and carriers with above average costs can charge higher rates if they can provide data to justify those higher rates. On this record, it is clear that NECA's proposal is meritless and must be rejected.

No Section 214 Exemption Is Warranted For CMRS Carriers. International Section 214 authorizations are properly subject to greater scrutiny than that applied to domestic market entry because in addition to competitive concerns, they also may raise national security, law enforcement, foreign policy and trade policy concerns.[104] The streamlined international Section 214 application process allows the Commission to address any such concerns, while imposing minimal burdens on applicants. The Commission accordingly should reject the request by

[103] *See* National Telephone Cooperative Association's Petition For Reconsideration*, Implementation of the Telecommunications Act of 1996; Telecommunications Carriers' Use of Customer Proprietary Network Information*, CC Docket Nos. 96-115, 99-273 (filed November 4, 1999).

Cingular (at 5-7) for the exemption of CMRS carriers from Section 214 and Part 63 international rules.

Cingular's claim that potential public interest concerns requiring Commission or Executive Branch scrutiny do not apply to CMRS providers that resell international services is belied by the Commission's *Voicestream Order*, which imposed Section 63.10 dominant carrier safeguards "to prevent vertical harms by the merging parties" and to "provide additional confidence that DT will not have the ability to engage in cross-subsidization with respect to international services provided by its U.S. affiliates."[105] That approval was also conditioned on compliance with additional conditions to address concerns raised by the Department of Justice and the Federal Bureau of Investigation that the transfer of control of this CMRS provider "would present significant impediments to the ability of the U.S. government to preserve national security, enforce the laws, and protect the public safety."[106]

Equally flawed is Cingular's alternative request (at 8) to extend the Section 63.21(i) exemption allowing authorized carriers to provide service through wholly-owned direct or indirect subsidiaries to include "wholly-controlled" CMRS subsidiaries (*i.e.*, those with minority ownership interests). As the Commission found in rejecting a similar request in the 1998 Biennial Review, "a controlling interest that does not amount to 100 percent ownership may raise additional issues, such as additional foreign affiliations or minority ownership or beneficial

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[104] *See Foreign Participation Order,* 12 FCC Rcd. 23,891, ¶¶ 47-66 (1997); *Market Entry and Regulation of Foreign-Affiliated Entities*, 11 FCC Rcd. 3873, ¶¶ 171-72 (1996).

[105] *Voicestream Wireless Corp*., 16 FCC Rcd. 9779, ¶ 102 (2001) ("*Voicestream Order*"). *See also*, 47 C.F.R. Sect. 63.10(c) (listing dominant carrier safeguards applicable to international resale carriers affiliated with foreign carriers that possess market power).

[106] *Id*. ¶¶ 73-77.

interest by persons or entities who are barred from holding a Commission authorization."[107] Moreover, Cingular would effectively exempt CMRS carriers with less-than-controlling, above-25 percent foreign carrier ownership interests from a broad range of Commission rules and policies governing CMRS carriers affiliated with foreign carriers.[108] Cingular shows no basis for exempting CMRS carriers from these Commission rules and policies preventing the leveraging of foreign market power into the U.S. market.[109]

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[107] Report and Order, *1998 Biennial Regulatory Review – Review of International Common Carrier Regulations*, 14 FCC Rcd. 4909, ¶ 56 (1999).

[108] *See, e.g.*, 47 C.F.R. §§ 63.09 (e) (25 percent affiliation standard); 63.10 (dominant carrier rules); 63.11 (affiliation notification requirement); 63.12(c)(1) (eligibility for streamlined treatment); 63.18 (k) (effective competitive opportunities test for non-WTO Member countries). *See also* Report and Order, *Market Entry and Regulation of Foreign-Affiliated Entities*, 11 FCC Rcd. 3873, ¶ 80 (adopting over-25 percent affiliation standard, rather than control standard, because "a less than controlling interest can provide a carrier with the incentive and ability to engage in anticompetitive conduct").

[109] Winstar (at 4) urges the Commission to request from carriers data relating to the availability of private lines that offer two-way, high speed connectivity. Winstar's proposal is beyond the scope of this proceeding, the purpose of which is to eliminate outdated regulations and not to adopt new rules. Such data reporting is already the subject of a pending Commission rulemaking (*see* FCC 00-114). Moreover, as AT&T already has shown in that proceeding, the requirement Winstar advocates here would be unduly costly and burdensome for regulated companies – the exact antithesis of the Commission's objective here.

CONCLUSION

For the forgoing reasons, the Commission should reject the ILEC proposals to reduce accounting safeguards and to undermine a host of other regulations that continue to serve the public interest and are designed to protect consumers and competition from market power abuses.

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CERTIFICATE OF SERVICE

The undersigned hereby certifies that a copy of the foregoing Reply Comments of AT&T Corp. was served, by the first class mail, unless otherwise noted, the 4th day of November, 2002, on the following:

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